



Stemming the Tide of Foreclosures in Latino Communities

Presented at:

Using FHA for Housing Stabilization and Homeownership Retention

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Submitted by:

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My name is Victor Burrola, and I am the Director of the NCLR Homeownership Network (NHN) for the National Council of La Raza (NCLR), the largest national Hispanic civil rights and advocacy organization in the U.S. dedicated to improving opportunities for Hispanic Americans. I have been working on issues important to low-income families for nine years, and in this role I am responsible for overseeing the technical assistance, training, grants management, and quality control for our 50 housing counseling grantees. I also manage our relationships with lenders, servicers, and other key industry stakeholders.

I thank Chairman Frank and Ranking Member Bachus for inviting NCLR to share our views on this matter. The rising rate of foreclosures is one of the most pressing civil rights issues before us today. Homeownership, historically, has been an important tool used by working-class families to move into the ranks of the middle class. Losing their home means losing the opportunity to send their children to college, save for retirement, and pass wealth on to the next generation.

For more than two decades, NCLR has been committed to active engagement in public policy issues that focus on supporting strong fair housing and fair lending laws, increased access to financial services for low-income people, and promoting homeownership in the Latino community. Ten years ago, NCLR created the NCLR Homeownership Network (NHN). As a network of almost 50 community-based counseling providers, NHN works with more than 30,000 families annually. Since inception, NCLR has helped more than 25,000 families become first-time homebuyers. NCLR's subsidiary, the Raza Development Fund (RDF), is the nation's largest Hispanic Community Development Financial Institution (CDFI). Since 1999, RDF has closed 175 loans totaling more than \$94.5 million while leveraging more than \$500 million in financing for locally based development projects in 21 states, building the capacity of local nonprofits and creating opportunities for Latino communities. These relationships have increased NCLR's institutional knowledge of how Latinos interact with the mortgage and financial markets, and how that interaction affects their communities.

We commend Chairman Frank for his ongoing work to ensure the American dream of homeownership for millions of Americans. NCLR believes that the "FHA Housing Stabilization & Homeownership Retention Act" would take significant steps toward stemming the tide of foreclosures and easing the burden on neighborhoods. As you well know, many families facing foreclosure today could afford to pay a mortgage if it were affordable. However, as victims of negligent underwriting and predatory lending, they now face mortgages that are wildly unaffordable. Modifying the terms of mortgages for borrowers who are able and willing to pay is the most efficient way to address the crisis.

In dealing with dozens of different housing markets throughout the country, NCLR has developed a keen sense of what community organizations need to respond effectively to the crisis before them. In my testimony today, I will discuss those needs, as well as the ways in which the proposed legislation addresses their challenges. I will conclude by making recommendations for improving the legislation.

Background

Many Latino families face significant barriers to sustainable homeownership. Their unique borrower profiles – such as multiple wage earners and thin credit histories – make them unattractive to many lenders who rely heavily on automated underwriting. Subprime lenders move quickly to fill the gap between market demand and services provided. As a result, Latinos and African Americans are often steered toward the products most profitable to the lender, but which may be expensive and risky for borrowers, regardless of their creditworthiness. Research shows that Latinos are 30% more likely than Whites to receive a high-cost loan when purchasing their home. Other research shows that nontraditional mortgage products such as Option Adjustable Rate Mortgages (Option ARMs) and interest-only mortgages are disproportionately concentrated among minority borrowers; Latinos are more than twice as likely as Whites to receive an Option ARM.

Early in 2007 NCLR joined other members of the Leadership Conference on Civil Rights (LCCR) Housing Task Force in calling on the industry to institute a six-month moratorium on foreclosures for families with the riskiest subprime loans – those with payment shock. A moratorium on this select group of foreclosures would give all parties involved time to identify meaningful resolutions. Our public call not only was met with skepticism, but we were also told that the market would soon correct itself. Not only has the market not corrected, but it continues to worsen. While forecasters are predicting 1.8 million foreclosures in 2008 alone, NCLR is concerned that the height of the crisis for Latinos will not come until 2009 and 2010, when Option ARMs and interest-only loans are scheduled to reset.

For most Americans, homeownership is their first step toward building the kind of long-term wealth that will allow them to send their children to college, save for a secure retirement, and provide for their family in times of unexpected financial emergency. In 2006, Latino homeownership reached an all-time high of 49.7%. Unfortunately, rising foreclosure rates in Latino communities threaten to erode these gains. All Americans rely on financial products to help them buy homes and otherwise build wealth and financial security. Our country cannot afford to leave these families behind, or to ignore the structural barriers that continue to marginalize minority borrowers, preventing them from building long-term sustainable wealth.

Needs of the Latino Community

Through NHN, NCLR has been working in low- and moderate-income Latino communities for more than ten years. After helping more than 25,000 families become homeowners, we have learned what it takes to connect low-income, low-wealth, and immigrant families with sustainable homeownership opportunities. Three years ago we began funding our network to provide foreclosure prevention counseling as well. Through this work, we have gained insight and understanding into the needs of Latino and minority communities neglected by mainstream banks and pummeled by foreclosure, as well as the needs of the community organizations that serve them.

Allow me to begin with a story of one of our clients from rural north Georgia. The Hera family came to visit one of our member groups, Dalton-Whitfield Community Development Corporation (DWCDC). With their hours cut at the local factory, the Hera family qualified for a hardship loan modification – one of the most noncontroversial kinds. All paperwork was properly submitted to the servicer, but the company never responded to their request or returned phone calls by DWCDC. The home was days away from being auctioned, when the lender contacted the agency with the news that they would accept the modification terms, but the family had to come up with an additional \$2,000 to cover the legal costs incurred as a result of the property moving to auction. The couple had already scraped together all their savings to pay two months of back payments, as required by their modification. Because of the servicer's delays, the family's plan became unaffordable. They lost their home through a foreclosure auction.

The story of the Hera family is indicative of what we are seeing throughout the country. Loan modifications are not happening at the wholesale level needed to save families from foreclosure. While many in the industry point to statistics stating that many families in foreclosure never reached out to their servicer, our experience is that servicers often cannot respond to borrowers or counseling agencies in a manner adequate to avoid foreclosure.

In addition to delays and capacity challenges with servicers, community-based organizations (CBOs) face five distinct challenges in their work to save families from foreclosure.

- **Voluntary loan modification programs are not working.** Our housing counselors receive hundreds of calls each week from borrowers desperately seeking help in saving their home. Despite the hard work of well-trained housing counselors and the eagerness of families to resolve their situation, we are not seeing the kind of loan modifications necessary to keep families in their homes. There are several factors contributing to the stalemate. First, borrowers with “piggyback” second loans oftentimes discover that the second lender/holder is unwilling to negotiate the terms of the loan, tying the hands of all involved. Another factor is the capacity of servicers to review each delinquent borrower's case and make a determination as to whether they meet the eligibility requirements for a modification. Moreover, servicers are relying heavily on short-term payment plans that last three to six months. This is just a band-aid; the mortgage will be just as unaffordable for that family when the plan expires.
- **More capacity and support is needed.** We thank the members of this committee who have been strong proponents of the Department of Housing and Urban Development (HUD) Housing Counseling Program. Continued support for this program is necessary. It is our understanding that the Neighborhood Reinvestment Corporation (NRC), recipients of \$180 million through the fiscal year 2008 HUD Consolidated Appropriations Act, received requests totaling \$340 million. We cannot underestimate the demand for housing counseling services. Not only is the demand for housing counseling increasing, but demand for related services is skyrocketing. Homeless shelters, mental health professionals, and legal aid organizations cannot keep pace with their increased client volume. Moreover, the rising number of people looking for affordable rental homes adds to the burdens of an already fragile market.

- **Foreclosure rescue scams are competing with legitimate housing counseling agencies.** Troubled borrowers, many of whom have already been victimized by predatory lenders, are fast becoming the targets of fraudulent foreclosure rescue scams. Borrowers desperate to save their homes are easy targets for predatory lenders who present themselves as “foreclosure consultants” and make unrealistic promises to save the home from foreclosure. Many victims feel as if they have few options and are pressured into signing papers they do not understand. Predators commit to refinances or temporary transfer of deeds in which the family believes they will rent for a short period of time and earn their way back to ownership; others completely misrepresent the documents the client signs. Yet others pose as disinterested parties offering to negotiate with the lender/servicer on behalf of the borrower. In most cases, the contract is written with terms so burdensome it is unlikely that the family will ever be able to recover its home or benefit from the sale of the property. We see not only an uptick in this type of activity, but also unemployed real estate and mortgage professionals heavily recruited into this field with the promise of high commissions.
- **Neighborhoods are in decline.** A growing number of communities are struggling to keep up with the growing number of vacant and abandoned homes. This phenomenon is especially prevalent in minority communities where risky mortgages are concentrated. Vacant and abandoned properties lower neighboring property values, become safety hazards to the community, and pose serious costs to municipalities in the form of maintenance and lost tax revenue. Many cities not only lack the funding to maintain the properties, but many also lack the necessary technical expertise to address the problem.
- **Ownership opportunities are drying up.** With mortgage rates at their lowest point in years, many families may be able to purchase a home with the assistance and protection of affordable homeownership programs. We have serious concerns, however, about the credit crunch and its impact on the ability of mortgage-ready families to purchase a home. For example, we have heard reports from the field that the Federal Housing Administration (FHA) is no longer insuring mortgages for zero credit score borrowers. As mentioned above, 22% of Latinos do not have credit scores, but most can still demonstrate their creditworthiness by documenting on-time rent and utility payments. Other lenders are putting similar policies into place, along with so-called “Declining Markets” policies that raise Loan-to-Value (LTV) ratios in certain neighborhoods.

“FHA Housing Stabilization & Homeownership Retention Act”

NCLR applauds Chairman Frank and others who worked on this bill for putting out an aggressive legislative plan to save the homes of thousands of families. Generally speaking, NCLR is supportive of the concepts included in the bill. We would like to discuss three areas of the bill which we think are critical to our communities, as well as three areas where we have some concern. The three provisions we believe are critical to maintain in the final legislation are:

- **FHA insurance for mortgage retention.** Title I of the proposed bill is the heart of the legislation. As stated above, troubled borrowers are not able to access loan modifications

that emphasize long-term affordability. Without the ability to modify or refinance their existing mortgage, most families will not be able to avoid foreclosure. While we have some technical concerns, discussed below, there would be no real relief for troubled borrowers without this provision.

- **Flexible underwriting.** NCLR strongly supports the flexible underwriting standard in Title I. As previously described, many borrowers currently facing foreclosure find themselves in such a position through no fault of their own. NCLR has serious concerns about the long-term impact of predatory lending on minority families' credit, and therefore on their ability to access important financial products. Instructing FHA to look past any delinquency or default when underwriting the new mortgage not only opens the doors to this program to more families, it also helps predatory lending victims begin to rebuild their credit.
- **Loans and grants for purchase of foreclosed homes.** As described above, neighborhoods are struggling to keep up with the challenges created by vacant and abandoned properties. The concept of extending a combination of loans and grants to states and cities to address this issue is one that NCLR supports. Cities require flexible dollars to address the fallout from foreclosure according to their market needs.

In addition, there are three areas where we have some concern. These are:

- **Lack of capacity to pay standard is too strict.** The bill proposes a mortgage debt-to-income (DTI) standard of 40% as a criterion for establishing lack of capacity to pay the existing mortgage, and requires that this standard be met as of March 1, 2008. NCLR is seriously concerned that this will block thousands of Latino families from the program. The focus on mortgage DTI is too narrow and would fail to capture the entirety of the borrower's circumstances. HUD has long held the standard that paying more than 30% of a family's income toward housing is considered unaffordable. Residual income should also be a consideration. Moreover, as we describe above, we are concerned that the peak years for foreclosures among Latino borrowers will be in 2009 and 2010, when Option ARMs and other Alt-A products are predicted to reset. Therefore, the cutoff date of March 1, 2008 would leave a significant segment of the Latino community out of the program.
- **Timing will be an issue.** While we understand the goal of being efficient and accountable with the funds made available under this program, we are concerned that some of the timelines set out in the bill are too strict. For example, Title I eligibility criteria state that only borrowers whose loans were originated between January 2005 and July 2007 would qualify. In certain markets, Alt-A mortgages such as Option ARMs and Interest-Only loans were still being originated. Many of these loans were subject to the same negligent underwriting used in the subprime market, and many of the borrowers will be exposed to the same kind of payment shock. In addition, we are concerned about the sunset provision in Title I. With FHA taking on the ultimate role of arbiter in the transaction, questions arise as to its capacity to handle the pace and volume of mortgages which the market will demand. With regards to Title III, we believe the two-year sunset, as well as some of the short-term deadlines with the states, are not practical. As noted above, research shows that Option ARMs and other Alt-A mortgages are expected to reach their peak level of resets in 2009

and 2010. Therefore, we are expecting the need for neighborhood stabilization and property acquisition, rehab, and sale to continue for several years past the sunset.

- **The stabilization fund presents operational challenges.** As an organization involved in both the lending and development side of housing rehabilitation work, NCLR has three concerns about how the fund will work. First, as stated above, the narrow timeline outlined for states, including creating a plan, identifying designees and properties, and distributing funds, is too strict. If left unchanged, the bill lends itself to large investment corporations that specialize in turning over Real Estate Owned (REO) property. While the investment firms may be able to deliver scale, they are not necessarily skilled in community development, housing counseling, or retail sales at the local level. Past experience with such wholesale asset disposition activities, such as those of the Resolution Trust Corporation (RTC), has taught us that property management (when homes do not sell fast enough) becomes an important part of the equation. Thus, we believe this bill fails to recognize the critical roles of neighborhood Community Development Corporations (CDCs) and other CBOs that specialize in local development and have an active pipeline of families who are being prepared through housing counseling programs to purchase property. With their involvement, neighborhoods will be more likely to be repopulated by local families, whether through rental or ownership, rather than by outside investors. Finally, we are concerned that the small proportion of grant funding, relative to loan funds, favors, again, large investment firms. If the grant funding is insufficient to cover the costs of maintenance, rehab, downpayment assistance, and sale – as we believe it is – then the incentive is for the firms to hold the properties until the market improves and they can recapture more of their costs.

Recommendations

- **Extend the eligibility cut-off date.** Unless Congress extends the cut-off date for demonstrating a mortgage as unaffordable, thousands of Latino and other Alt-A borrowers will be left out of the program. NCLR strongly urges the committee to extend the cut-off date to December 2010.
- **Allow for more flexible timelines.** Titles I and III have two-year sunset provisions. In both cases, NCLR urges the committee to extend these to five years. This will allow more time for the market to play out and to ensure that all eligible communities and borrowers are able to access the program.
- **Create two separate funding streams for nonprofits putting families into rehabbed homes.** Local CDCs and CBOs have an important role to play in resuscitating neighborhoods from the damage created by foreclosure. So that neighborhoods are not held captive to outside investment warehouses, NCLR recommends that Congress create a set-aside for qualified local nonprofits that could be responsible for the program marketing, counseling, and loan qualification for qualified families. REO contractors would rely on this pool of qualified borrowers for their unit sales. This way, Congress can ensure that some portion of the funds will be spent locally and through organizations that directly serve the interest of the community.

- **Investigate foreclosure rescue scams.** NCLR calls on members of the House Financial Services Committee to hold a hearing on investigating foreclosure rescue scams. Not only are these fraudulent services competing with legitimate HUD-certified housing counselors, they are also likely to be a direct competitor for the FHA program proposed in this legislation.